April 2013

When Europe Hits Home: How Europeanization Triggers the Conflict of Capitalism in the German System of Corporate Control

Alexander El Alaoui

University of Potsdam, Germany, lux.elalaoui@googlemail.com

Follow this and additional works at: http://scholarship.claremont.edu/urceu

Part of the Business Organizations Law Commons, Economic Policy Commons, International Business Commons, International Economics Commons, and the Political Economy Commons

Recommended Citation
Available at: http://scholarship.claremont.edu/urceu/vol2012/iss1/8

This Chapter is brought to you for free and open access by the Journals at Claremont at Scholarship @ Claremont. It has been accepted for inclusion in Claremont-UC Undergraduate Research Conference on the European Union by an authorized administrator of Scholarship @ Claremont. For more information, please contact scholarship@cuc.claremont.edu.
When Europe Hits Home: How Europeanization Triggers the Conflict of Capitalism in the German System of Corporate Control

Alexander El Alaoui
University of Potsdam, Germany

ABSTRACT
This paper challenges the methodological adherence to institutional stability of the “Varieties of Capitalism” approach by showing that constant change pressure caused by ‘negative EU integration’ has, indeed, profoundly affected the German system of corporate control. Over the past years, European institutions have been striving to create a common market for corporate control in order to make the EU the world’s most competitive economic area. Europe’s push for liberalization, however, has not only affected the German system of corporate control itself, but also undermined patterns of the German financial system and system of industrial relations. Building on the assumption of institutional complementarities it is argued that if adjustment pressure is put on one element of a country’s political economy, other parts will not remain unaffected. Will the German coordinated market economy converge towards a more liberal capitalist system?

KEYWORDS
Varieties of Capitalism, Europeanization, corporate control, Germany
For a half-century after its emergence during the post-war construction period, the German political economy was notably stable and resistant to any form of substantial reform pressure. Notwithstanding economic turbulence in the 1970s and 1980s, Germany celebrated itself as an “island of economic prosperity” (Kitschelt & Streeck, 2003, p. 1) and successfully managed to bridge principles of social protection and free market rule (Soziale Marktwirtschaft). The “middle way” (Schmidt, 2001) between a Scandinavian welfare state and Anglo-American turbo capitalism (Leibfried & Obinger, 2003, p. 199) laid the groundwork for a well-functioning economic system often referred to as the “German Model” (Esser, 1996). In the 1990s, however, this harmonious picture started crumbling. As soon as Germany was exposed to greatly increased international competition and the globalization of markets, its institutions suddenly were faced by growing adjustment pressure.

It comes as no surprise that the reshaping of German capitalism has been thoroughly discussed by the scholarship of the past twenty or so years. Most research suggests that internationalization – a term often remaining vague – has forced the German nation state to recalibrate its market equilibrium according to Anglo-Saxon standards, a process which has affected a wide set of the political economy’s basic elements. Another approach, though, traces domestic change back to the effects of European integration. While this concept is put forward by far fewer studies, I argue it might serve as a much better conceptual gateway of change than internationalization alone.

Building on the notion that “Europeanization”, in fact, has led to the erosion of German capitalism, I aim to highlight the role of EU integration in reshaping the German political economy, and thus call the stability-hypothesis of the “German Model” into question. Furthermore, I aim not only to bring the study of Europeanization “back to the table”, but also to situate it within the debate on the “Varieties of Capitalism” (or VoC). Both approaches still stand apart from each other despite their common focus on the question of whether a clash of systems might initiate a process of convergence (Callaghan, 2010). In other words, I assume that the EU’s push for liberalizing national markets does not coincide by accident with Germany’s partial system change, which is commonly captured by the VoC literature.

The VoC approach allows one not only to analyze what aspects of the German political economy seem to have been “under attack” by EU integration, but also to link those change processes with one another. In fact, many developments within the architecture of German capitalism have been addresses separately by scholars when they should have been analyzed jointly. Accordingly, I argue in favor of an analysis that de-centers the study of change from a narrow focus on either element and that sets them in relation to each other. The hypothesis underlying this study is that Europeanization will lead to the creation of a market for corporate control that will alter basic principles of both the financial system and industrial relations.

The study proceeds as follows: Part one sets out the analytical framework along which the German political economy can be classified. This is followed by a brief outline of the discussion on convergence and concluded by the idea that some form of cohesion among political economies is to be expected considering the high degree of pressure for liberalization. Section three illustrates the argument with a short description of why Europeanization is the gateway of change, followed by two case studies in part four. The conclusion highlights the key results of and sums up the most striking findings from the previous sections.

1. Varieties of Capitalism and Institutional Complementarities

Capitalism versus capitalism – For decades scholars have been intrigued by the question...
why diversity among capitalist systems exists and to what degree this diversity accounts for a country’s economic performance. At some point in the 1950s, research ceased to suggest unanimously that capitalism’s only counterpart was not communism, but capitalism itself. The first to study capitalist diversity was Andrew Shonfield who in his book “Modern Capitalism” (1965) compared several world economies, including Great Britain and Germany, and laid out why some countries did well while others lagged behind. Quickly, literature on the “models of capitalism” mushroomed. Inspired by Shonfield’s widely noticed study, French author Michel Albert took up the idea of a bipolar world of capitalism and suggested a distinction between a ‘Rhenish-Alpine-Japanese’ and a ‘neo-American’ model in his 1993 “Capitalism vs. Capitalism”. This approach was picked up more recently by Hall and Soskice’s (2001) often quoted “Varieties of Capitalism”. In the latter, capitalist diversity across nations is conceptualized along two basic types of political economies, the liberal (LME) and coordinated market economy (CME), which differ by reference to the way in which firms resolve coordination problems.

In this study, I will borrow from Hall and Soskice’s VoC approach and regard Germany as a paradigm case for a CME. Unlike other studies, though, I do not seek to assess the strengths and weaknesses of either system but to analyze why and how one system might converge towards its assumed counterpart. In the subsequent paragraphs, I will provide a brief introduction into the VoC concept and portray its most essential features.

The VoC approach builds on the assumption that cross-national variations in economies may be best traced back to institutional differences among CMEs and LMEs. In coordinated market economies like Germany, firms coordinate their endeavors through non-market mechanisms such as corporate networks (inter-firm- and bank-client networks) and institutionalized negotiations (tripartite rounds and bilateral wage bargaining). Established arrangements and long-term inter industry relationships are said to allow for stable production structures that are less sensitive to changing market conditions. In liberal market economies, in contrast, supply and demand of goods and services is balanced through price competition rather than “close-knit corporate networks” (Hall & Soskice, 2001, p. 29).

It is noteworthy that the “models of capitalism thought to generate comparative (...) advantage[s] are not just random configurations of rules but display so-called institutional complementarities” (Callaghan, 2010, p. 567). Referencing work in economics, it is assumed that institutional complementarities reinforce basic differences between CMEs and LMEs. The extensive use of highly trained workforces in CMEs, for example, is backed up by a sector-specific vocational training system tailored to the corresponding firms’ needs (see section four for details).

The interplay of institutional complementarities, according to the ‘Varieties approach’, generates certain comparative advantages which lay the groundwork for firms to engage in a specific production system. Keeping to the above example, a firm will specialize in the production of cars and heavy machinery as long as it can do so in a more efficient way than others. Efficiency in this kind of production may result from the access to highly qualified workers, as is the case in Germany. Simply put, firms will engage in a way for which they receive ‘institutional support’, which is why a system that has once set on a path will not easily deviate from the status quo without further incentive.

Now, there is one good side to this line of argumentation and one that needs to be revised:
i. Institutional complementarities not only allow for a stable production regime, they also serve as an analytical tool to examine interdependencies between one element of a political economy and another. In part four, I will make extensive use of this tool.

ii. According to Hall and Soskice, institutional path dependency will make system change impossible and a fortiori rules out that one system might converge towards the other. However, empirical evidence will prove this not necessarily to be true.

To sum it up, capitalist systems differ with regard to the institutional setting they are built on and are thus often believed to be fairly resistant to adjustment pressure. Opposing this view, I will follow recent research and argue that change is not only possible but is actually happening. Hence, the next section will outline under which circumstances system change is to be expected.

2. THE STUDY OF CHANGE: CONVERGENCE AND LIBERALIZATION

Over the past few years, the focus of debate among scholars has shifted to one question: Will international integration drive all economies towards one market model that will absorb all previously existing market equilibriums? Against this notion, some believe that institutional stability, which is key to the understanding of capitalist diversity, will shield systems from any external threat, be it globalization or Europeanization. They argue that procedures, rules and norms that shape market organization are backed up by a social bloc, which would not easily withdraw its support. As outlined above, this is so because firms, which are the single most important actor, rely on one or the other form of market organization since they are intertwined with the existing institutional setting. In short, there is little room for abrupt adjustment. Other scholars, however, oppose this view by pointing out recent developments, such as the increase of investment banking, shareholder value, new accounting standards and short-term investments. All of these examples suggest that firms are slowly yet surely shifting towards the Anglo-American business model. Clearly, the literature at hand does not have a unanimous view on the issue of convergence.

Now, it is vital to bear in mind that systems in historical perspective have always been subject to change. Throughout the world, political economies have manifested themselves as hybrid models rather than monolith blocs. As Gourevitch (1996, pp. 240-241) shows, there was a time when US-capitalism had significant elements of the Rhenish model and when Japan moved to become a system most akin to that of Germany. Furthermore, according to the study of Europeanization, there is little reason to believe that traditions regardless of their persistence should be completely immune to either domestic or international forces.

While one can therefore reasonably assume that a political economy might partially change, it is a fact that the congruence-hypothesis remains far too often unclear with regard to definition: Convergence; but where to? Will there be one ‘best-practice’ system all the others will gravitate toward? Or will both CMEs and LMEs somehow synthesize and create some form of a mixed type? In fact, scholars have advocated both approaches and underpinned their argument with empirical findings. For the sake of clarity, however, I will define convergence as “a process in which a CME is forced to absorb substantial elements of its LME-counterpart in order better to fit the globalized economic order”. Interestingly enough, support for this notion comes from the “Varieties of Capitalism” itself. While Hall and Soskice deny ‘congruence’ as
a matter of principle, they acknowledge transformation in some instances: “Because market relations do not demand the same levels of common knowledge, however, there is no such constraint on CMEs deregulation to become more like LMEs” (Hall & Soskice, 2001, p. 63). With this, they confirm scholarly expectations according to which liberalization does promote change.

**Liberalization: The trigger of change?**

As follows from the last sub-chapter, congruence, if it occurs at all, may result from the process of liberalization of coordinated market economies. In most studies, it is argued that the inflow of Anglo-American business rationales – a side effect of market opening measures – challenges systems of organized capitalism and thus causes adoption. This phenomenon is sometimes referred to as the “rise of the phoenix” (Cohen, 1996) connoting the dramatic resurrection of global finance after World War II. As a result, CMEs may find themselves in a process of metamorphosis, gradually turning into their counterpart and increasingly being blown off their former path.

Liberalization, however, does not arise from nowhere nor is it a random effect possibly caused by globalization. It is a self-induced, bottom-up initiated and moderated intervention in an existing order, directed at removing obstacles to trade, competition and market integration. To this extent it would be a narrow view to assume that some ‘external’ developments threaten CMEs. It is rather the interplay of domestic and international factors that underpin change. In the case in question, indeed, the gateway of liberalization is Brussels As Schmidt (2002, pp. 39-41) points out, “changes related to globalization cannot be considered in isolation from those related to the regionalism concerning European integration. (…) Europeanization has been inextricably linked to globalization in the set of liberal, capitalist ideas”.

### 3. Gateway of Change: Europeanization

The recalibration of German capitalism can hardly be traced back to one single factor only. Rather, evidence suggests that the orientation towards a greater market economy is affected by “simultaneous and reciprocally reinforcing, complementary developments (Beyer & Höpner, 2003, p. 180). Thanks to a large number of studies we know a great deal about the factors underpinning the change process, while the plethora of approaches, at the same time, makes it difficult to identify the factors that really cause change. According to Höpner (2001), scholars have suggested three main gateways of Anglo-Saxon production-system elements: financial internationalization, shareholder value orientation (Höpner & Schäfer, 2010) and domestic factors (Kitschelt & Streeck, 2003).

All of the above approaches suggest that adaptation pressure, when constantly exerted on the nation state, will inevitably lead to the exhaustion of organized capitalism and consequently give rise to the erosion of its institutional basis. In fact, I assume that one or more of these processes do take place and above all, work in tandem. Far too rare, however, are the attempts to construct an analytical framework that seeks to capture the manifold mechanisms in one comprehensive concept. Accordingly, drawing on latest research, I advocate shifting the focus away from “internationalization” towards the effects of European integration on organized capitalism (see Höpner & Schäfer, 2010). This approach builds on three assump-

---

1 Liberalization usually refers either to the reduction of government interference in market processes or to deregulation policies aimed at strengthening private entities.
tions, which will be set out in the following sections:

i. Europeanization is a *sui generis* case of internationalization

ii. Europeanization actively promotes market opening (‘negative integration’)

iii. Europeanization aims at harmonizing systems of corporate control

In short, the Europeanization hypothesis does not substitute mechanisms commonly referred to as internationalization, nor does it suggest that other mechanisms are not at work. As has been argued earlier, domestic transformation is a multicausal process that involves a whole set of both internal and external factors with each of them reinforcing each other. The Europeanization hypothesis, though, seeks to add another perspective to the debate on the varieties of capitalism as it argues that the push towards congruence did not randomly come about but was rather actively fostered.

**3.1. Europeanization, internationalization, and liberalization**

In its simplest sense, Europeanization may be defined as a *sui generis* case of internationalization. While the latter refers solely to the opening of national markets along with the “increase in cross-border transactions, social relations and structures” (Bouwen, 2006, p. 178), Europeanization adds a dimension of “obligation”. Simply put, “Europeanisation is (…) a process of domestic political change caused (somehow) by the process of European integration” (Vink, 2003, p. 72). Unlike other international regimes, though, the European Union has been equipped with a large arsenal of supranational controls over public policy, making EU officials capable of enacting legislation that is binding on the member states. This, however, distinguishes the EU from any other form of transnational cooperation, which usually builds on voluntary agreements. “[W]hether a decision comes out of treaty negotiations, Council directives, or of the ECJ, once it is decided it becomes an adjustment pressure for all member state since all must implement the decision” (Schmidt, 2002, p. 86). It is for that reason that Europeanization appears to be a better conceptual gateway of liberalization than globalization or internationalization only.

**3.2. Europeanization and the early phase of ‘negative integration’**

The link between European integration and liberalization arises from the EU’s past. Ever since its emergence in the 1950s, the European Union (or formerly European Community, EC) has constantly been rebuilding itself. While the EU’s founding principles were built on the vision of a *political* unity and cooperation (e.g., ‘Schuman plan’) they have been undermined by the strengthening of the economic direction of further integration that political elites have stressed in the 1960s. Many argue that with the creation of the single market Europe has been blown off its path to a political union and recent developments provide striking evidence for this. However, Europe’s push for liberalization did not arise accidentally but resulted from the failure of macroeconomic management during the economic turmoil of the 1970s and 1980s. In the search for a political solution to the crisis EC authorities implemented corporatist mechanisms, as they were believed to boost economic

---

2 The literature on Europeanization most commonly points to domestic change in cases of national nonconformity with European rules or norms. Accordingly, most scholars agree on the assumption that incongruence between the supranational and national level is the necessary condition for any form of adaptation pressure that originates from the EU (Sturm & Pehle, 2005; Börzel & Risse, 2000; Cowles, 2001). Likewise, the same mechanism is at work behind the ‘congruence-hypothesis’.

http://scholarship.claremont.edu/urceu/vol2012/iss1/8
growth and promote social stability. As the EU kept struggling with the economic situation and steadily failed to combat unemployment, those mechanisms were quickly repealed and decision-making power was shifted back to the domestic level3 (see Gorges, 1996, ch. 5 and 6; Streeck & Schmitter, 1991, pp. 143-145).

Finally, the poor economic performance of the EC’s key member states Germany, France and Great Britain raised popular doubts as to whether the ‘European idea’ was worth sticking to; in sum, “Euroscepticism” had its heyday. Hence, a further trigger of liberalization was ideological. The Anglo-Saxon market model enjoyed great popularity among European leaders during that time. Consequently, politics was driven by the idea of a new market-based economy that would be able to solve the problems of the past (Moravcsik, 1991).

As soon as it became evident that further steps towards more integration would be possible only with regard to economic harmonization, the vision of a political union began slowly to disappear. From that time on, the creation of a common European market was declared the primary objective of European authorities and soon the EC would become the world’s largest free trade zone. In 1986, the Single European Act (SEA) was ratified, which laid the groundwork for “the creation of a single market for (...) banking and insurance, a single legal framework for business (...) and the easing of restrictions on living and working in other member states” (Coen, 1997, p. 94). In the social sciences, this process is commonly captured by the umbrella term “negative integration”4, which denotes the removal of legal barriers such as custom duties that would interfere with free competition (Scharpf, 1999, pp. 43-84). Inherently linked to the creation of the single market is the free movement of goods, capital, services and people – the so-called “four liberties”. Finally, less than a decade later, authorities throughout the continent called for a common currency, the Euro, which was introduced slightly later as part of the European Economic Monetary Union (EMU).

From the early phase, the push toward liberalization was not only tolerated by national executives and parliaments but also actually actively promoted. To cite a case in point, Germany has been extensively practicing what the Europeanization literature calls an ‘institution upload’, which is to say it designed respective institutions of macroeconomic management such as the EU’s central bank (ECB) according to domestic experiences (Deutsche Bundesbank). For example, the “EMU (...) has been little more than an extension to Europe and its member states of Germany’s own traditional macroeconomic patterns and prejudices” (Schmidt, 2002, p. 90) and thus did not interfere with national politics. Furthermore, German actors ‘of all colors’ have been of outstanding importance for the “standard-setting in the European Single Market program” (Jeffery & Paterson, 2003, p. 61). Over the last fifteen years or so, the European Commission (COM) along with the European Court of Justice (ECJ) have profoundly challenged Germany’s organized capitalism by over-prioritizing undistorted competition in a way that is clearly diametrical to the past. In the words of Jeffery and Paterson (2003, p. 66), “[l]iberalization (...) now begins to hurt”.

3.3. Europeanization and the harmonization of corporate control

Traditional integration theory regards European institutions, particularly the COM and ECJ, as the “guardians of the Treaties”, the machinery behind integration and agents of

---

3 However, due to a lack of control over fiscal and monetary policy tools, “Euro-corporatism” was never really ‘properly’ implemented and might therefore have failed.

4 Positive integration, on the contrary, means the exercise of regulative competencies on the supranational level, which usually points to political measures that seek to ‘correct’ market forces.
national governments. Challenging this view, these institutions seemed to have emancipated themselves from the role of a passive “contractor” of integration and moved forward to become political actors. At least, this is what recent developments suggest (e.g., the ruling of the ECJ in the cases of “Laval” and “Viking”). With regard to liberalization measures, the COM and ECJ have clearly developed its own rationales as they pushed market harmonization towards a new equilibrium bypassing the old status quo. As Höpner and Schäfer (2010, p. 344) show, recent policies imply that the EU “aim[s] at transforming national institutions and bringing them in line with the Anglo-Saxon model of capitalism”.

From that time on, the COM and ECJ have set the “four liberties” above all else and set out to combat anything that might interfere with the goal of promoting free markets, even though it is national institutions that supposedly bar the way to progress. Over the last few decades, the Commission has launched a set of initiatives aimed at creating a market for corporate control, which would lay the groundwork for hostile takeovers and consequently undermine basic institutions of Rhenish capitalism in Germany and elsewhere. In 2004, for example, EU institutions agreed on the “Directive on takeover bids” (2004/25/EC), whose purpose is to harmonize takeover processes across member states while emphasizing the rights of shareholders. Only one year earlier, the COM had announced a communiqué entitled “Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward” (COM (2003) 284 final) in which the Commission stressed the importance to “actively co-ordinate the corporate governance efforts” (p. 16) of EU member states. The EC plan has been repeatedly criticized for its one-sided goal to adjust regulatory systems in CMEs without addressing the question of how deregulation might affect essential aspects of coordinated market economies, for example codetermination (Kluge, 2007).

While national agendas have always been in line with COM and ECJ regulations with regard to market liberalization, this symbiosis has fallen apart in the case of takeover liberalization (Höpner & Schäfer, 2008, ch. 4; Callaghan & Höpner, 2005). For the first time, national authorities became aware of the effect European legislation might have on the continuity of “their” capitalist systems. Confirming scholarly expectation, political leaders of organized capitalisms have opposed first drafts of the above mentioned EC directive (Höpner & Schäfer, 2010, pp. 354–357) as they might fear the loss of national peculiarities and comparative advantages and a too radical shift towards the Anglo-Saxon market model. Regardless of the political opposition that occasionally dropped in, organized capitalism across the EU indeed has changed.

It should be noted that the integration of capital markets and the creation of a market for corporate control are still in motion, meaning neither one of the two processes has been finalized. And yet, the EU makes no secret of the fact that only a fully integrated financial market will guarantee a real European common market (see for example EC “Economic

5 The status quo of European integration was established through the harmonization of product markets guaranteeing the free movement of goods and services. The European free trade zone encouraged countries to build on their ability to produce respective goods at lower marginal cost or, in other words, goods based on the principle of comparative advantages (Ricardian theory). As follows from Hall and Soskice’s VoC-approach, a Ricardian production regime coincides with a country’s distinct capitalist order, since comparative advantages reinforce capitalist diversity and thus promote institutional stability. Consequently, national peculiarities remained largely unaffected by Europeanization.


7 Accessible online, accessed online on Jun 16, 2012.
So why did we look at the role of EU integration in the process of market liberalization? The purpose of this section was to show why and how Europeanization – and not simply internationalization – has initiated or at least propelled the clash of capitalisms as it is (1) binding on the nation state, (2) more effective both in depth and magnitude, and (3) politically intended. Furthermore, I argued that liberalization measures, while initially self-induced, now begin to hurt. In light of the COM and ECJ becoming autonomous players in the supranational arena, one might ask dramatically: Have we opened the “box of Pandora”?

4. **Case Study: A Market for Corporate Control and its Effects**

In section three, I showed that the EU has strived to create a market for corporate control, which would interfere with existing patterns in CMEs. In this section, I shall analyze to what degree changes within the German system of corporate control may affect other parts of the political economy. This approach borrows from the assumption of institutional complementarities, saying that pressure for change directed at either element of a CME will provoke the whole system to change and finally promote convergence as defined earlier.

**Figure 1: Research design**

In the following case study, two elements of CMEs will be at the center of analysis: (i.) financial system and (ii.) industrial relations. Both of these are commonly considered essential aspects of the German political economy, but there have been only few attempts to associate them with each other (e.g., research undertaken by Martin Höpner; Vitols, 2001). On the one hand we observe changes within the financial system that have been often linked to the ongoing liberalization of world markets. On the other hand, the gradual erosion of industrial relations has been usually traced back to the “modernization” of society (e.g., Leif & Speth, 2003a, ch. 3.3; Wehrmann, 2007, ch. 8). This appears to be unsatisfactory for several reasons. Above all, capitalism and corporatism in the German state are inherently linked and need thus to be analyzed jointly.

4.1. **Corporate control and the financial system**

Corporate control denotes the way a company is run. Is it an autonomous unit of the economy, committed only to rational goals such as profit maximization and efficiency (in LMEs), or is it an entity interwoven into “close-knit corporate networks” (Hall & Soskice, 2001, p. 29), and thus committed to a stable production regime that generates profit only in...
the long-term (CMEs)? The way a company constitutes itself along these guidelines decides to what form of capital it will have access to and hence determines the “design” of the financial system. Conclusively, if the system of corporate governance deviates from its status quo, so will the financial system. To illustrate these interdependencies, I will first briefly set out key characteristics of each market model before drawing on past and recent developments that provide evidence for the notion that Germany’s financial systems clearly is in motion.

As touched upon on at some earlier point, in coordinated capitalism, industry and finance are marked by a high degree of collective functioning and a ‘classical’ banking concept\(^{10}\). Banks play the key role in corporate finance; they lend money, own stock and are intertwined with their clients’ management\(^{11}\). Firms usually maintain a long-lasting relationship to ‘their’ banks (Hausbankprinzip) and thus can rely upon the banks’ willingness to support longer term investment plans and grant low interest credits (Lütz, 2000, pp. 5–6). Banks assess a firm’s credibility based on internal information they gather in meetings of the supervisory board they hold a seat in, which is to say they take co-entrepreneurial responsibility in order to exert influence on the debtor’s standing; they become insiders. These business-bank ties result, among others, from the fact that especially small and medium-sized enterprises (SME) – accounting for a large proportion of German business – lack the ability to finance themselves through issuing shares on the capital market (Vitols, 1998; Deutsche Bundesbank, 2012, p. 23). Furthermore, basic opaqueness and a high level of discretion, which secures the confidentiality of business information, prevent banks from depending on short-term profit maximization and allow for farsighted investment strategies that emphasize long-term results (Lütz, 2000).

In LMEs, on the contrary, investors from outside the company decide whether or not to invest in a company based on publicly available balance sheet data. Accordingly, investments are made based on the value of a company on the equity market. Unlike CMEs, company leaders are not necessarily supervised by a board consisting of bank personnel, workers’ representatives and others, but are accountable only to the shareholders. If the management fails to constantly boost the value of the shares emitted on the equity market, this company might become subject to fusion or (hostile) takeovers. It follows from there that the main difference between the financial system in CMEs and LMEs is the degree of market capitalization with regard to a firm’s assets. A company may choose to finance itself either through bank credit (CMEs) or through the distribution of shares on the equity market (LMEs). In practice, of course, most firms do not rely on one form of capital only but consist of a mix of different inflows.

Now, as takeovers became more popular in Germany and a market for corporate control emerged, “classical elements” of the financial system began to fall apart. It all started in 1999, when the British telecommunication company Vodafone-Airtouch sought control of the German industrial giant Mannesmann and a spectacular takeover battle was initiated, which would shake the very foundations of the German economic system; a genuine “cul-

---

10 The term ‘classical’ refers to a bank’s traditional activities in retail banking and credit banking, as will be outlined at a later point.

11 The German industry and banking sector is traditionally marked by a high degree of corporate networks. Bank officials are often members of their clients’ management and supervisory boards and gain valuable insights into a company’s business concept and strategic planning. The involvement of bank personnel in corporate management opens access to important information (e.g., a company’s financial standing) necessary for assessing possible risks in granting credits.

http://scholarship.claremont.edu/urceu/vol2012/iss1/8
tural break” (Seidlitz, 2009). Over the subsequent years, a growing number of middle sized companies saw themselves confronted with a “wave of hostile takeovers” (Dohmen, Haw-raneck & Tietz, 2010) and feared becoming smashed by foreign competitors.

What is at stake here is nothing less than the core principles of corporate organization. As has been discussed by Beyer (2003), takeovers will “cut” the ties between firms and universal banks and thus change the way companies procure capital. The argument goes as follows: Banks that wish to benefit from the business with takeovers (M&A) have a strong incentive to leave the supervisory boards and decouple themselves from corporate networks. No longer does it seem appropriate for a private bank to take on co-entrepreneurial responsibility given that firms, as they begin to demand external financial resources, seek to enter the capital market and change their mode of corporate control according to LME-standards. Exemplarily, Beyer (2003, p. 126) cites a case in which the Deutsche Bank supported the German company Thyssen-Krupp in their endeavor to takeover a firm, while the bank was still part of that firm’s supervisory board and consequently a conflict of interest arose. Banks now become “financial intermediaries” slowly quitting the credit business and searching for new business areas to engage in, primarily in investment banking. This might seem the most notable effect behind the eroding of corporate networks, often referred to as the fall of the Deutschland AG (Streeck & Höpner, 2003; Höpner & Krempel, 2004). According to a survey published by the Max Planck Institute for the Study of Societies (MPifG) in 2000, roughly 46% of large German businesses had cut ties to their respective house banks. Only 32% of the companies surveyed indicated that they still maintained a strong relationship to their house bank (quoted in Beyer, 2003, p. 130 footnote).

Recent data provided by the German Federal Bank (Deutsche Bundesbank) supports the same notion. Based on a brief assessment of the macroeconomic financial accounts for Germany, it becomes apparent that the financing structure of German business has deeply changed over recent decades. Between 1980 and 2010 German banks across all sectors began to play a bigger role in international trade with securities and expanded their portfolios substantially.

Table 1: MFIs Assets, 1980 – 2010

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Securities from:</td>
<td>0.2</td>
<td>0.6</td>
<td>1.1</td>
<td>1.4</td>
<td>1.5</td>
</tr>
<tr>
<td>domestic issuers</td>
<td>0.19</td>
<td>0.59</td>
<td>0.85</td>
<td>0.9</td>
<td>0.9</td>
</tr>
<tr>
<td>foreign issuers</td>
<td>0.01</td>
<td>0.04</td>
<td>0.25</td>
<td>0.5</td>
<td>0.6</td>
</tr>
<tr>
<td>Loans to**:</td>
<td>2.4</td>
<td>5.5</td>
<td>5.9</td>
<td>6.8</td>
<td>7.4</td>
</tr>
<tr>
<td>MFIs</td>
<td>0.5</td>
<td>1.4</td>
<td>1.5</td>
<td>1.9</td>
<td>2.1</td>
</tr>
<tr>
<td>domestic</td>
<td>0.4</td>
<td>1.0</td>
<td>1.06</td>
<td>1.1</td>
<td>1.2</td>
</tr>
<tr>
<td>foreign</td>
<td>0.1</td>
<td>0.4</td>
<td>0.44</td>
<td>0.8</td>
<td>0.9</td>
</tr>
<tr>
<td>non-MFIs</td>
<td>1.4</td>
<td>2.7</td>
<td>2.9</td>
<td>3.0</td>
<td>3.2</td>
</tr>
</tbody>
</table>

Source: Deutsche Bundesbank (2012)

** book and unsecured credits; data from each December

According to Table 1, revenues from securities issued by both domestic and foreign suppliers increased more than sevenfold (from 0.2 to 1.5 trillion €) during that period.
Over the same time, in contrast, total revenues from loans only tripled (from 2.4 to 7.4 trillion €). The data provided shows a trend towards stock trading rather than an all-encompassing substitution of credit banking. However, the relative share of stock trading as can be inferred from Table 1 has risen from 7.7 to 17% between 1980 and 2010. It is even more striking that investments in securities issued by foreign traders has skyrocketed (from 0.01 to 0.6 trillion €), yet again denoting the banks’ global orientation.

As banks shifted away from the domestic credit business, firms started to raise capital from sources other than credit; in fact, “[t]he bank credit (…) has systematically become less important over the past 20 years” (Deutsche Bundesbank, 2012, p. 13). While internal funds (e.g., through classical bank credits) are still the major capital source of companies, the share of external funds, including credits from non-banks (e.g. investors, finance houses) has substantially increased. As Table 2 illustrates, the share of bank credits has not been constant over time. In 1991 MFI-loan liabilities accounted for 32% of the balance sheet of German business; twenty years later, in 2010, this number had dropped to 18%.

| Table 2: Nonfinancial Company Sector Outstanding Liabilities, 1991 – 2010 |
|-----------------------------|-----------------|-----------------|-------------|-------------|-----------------|
| Type of liability in Billion € | 2 042          | 2 519          | 3 891        | 3 944        | 4 718           |
| in % of total liabilities | Security other than shares | 1.8            | 2.3           | 1.4          | 2.7             | 3.1             |
|                             | Loans including: | 38.1           | 35.5          | 29.3         | 30.3            | 31.8            |
|                             | from MFIs*      | 32.0           | 28.6          | 22.7         | 20.9            | 18.0            |
|                             | from non-MFIs*  | 6.1            | 6.9           | 6.6          | 9.4             | 13.8            |
| Technical provisions       | 5.7             | 5.6            | 4.3           | 5.2          | 4.8             |
| Other liabilities including: | 24.4           | 21.1           | 17.0          | 17.6         | 17.8            |
| Commercial credits and advances | 17.1           | 14.8           | 10.5          | 11.3         | 12.1            |
| Shares                     | 30.0            | 35.6           | 48.0          | 44.1         | 42.6            |

Source: Deutsche Bundesbank (2012)

* MFI = Monetary Financial institution.

During the period in question, banks have been increasingly replaced by alternative creditors. At the same time, shares (from 30 to 42.6%) and bonds (from 1.8 to 3.1%) have become noticeably attractive to companies. In short, whereas external funds still rely hugely on ‘classical’ credits, they are increasingly demanded from creditors other than banks (non-MFIs). As soon as banks began to switch to investment banking and firms shifted away from credit business, the strong bank-entrepreneurial partnership began to fall apart.

4.2. Corporate control and industrial relations

In a similar way to the example given in 4.1., corporate control and the financial system...
are linked to each other, as are corporate control and industrial relations. This link results from the strong inter-firm relationship characterizing most CMEs. Unlike LMEs, firms in CMEs are not loosely coupled units that only strive for their own goals, but rather team players who maintain strong strategic partnerships with one another. They agree to commit themselves to mutual trust and to certain sector-wide agreements. As soon as corporate control is exposed to an opposing business rationale, the system of industrial relations cannot remain unaffected by this. Similar to the last section, I will first lay out the most crucial characteristics of industrial relations in Germany before analyzing how institutional complementarities account for the steady transformation of corporatism. Change takes place at all levels of corporatism, but only the meso- and micro-levels adjustment may be traced back to the opening of a market for corporate control.

Corporatism is a key future of coordinated market economies and this holds particularly true for Germany. Most literature distinguishes between three levels of corporatism: meta or macro (economy wide), meso (sector level), and micro corporatism (firm level) (Gorges, 1996). In general, corporatism denotes a system of social organization that involves associations of homogenous interests into corporate groups, such as labor and business, which take part in tripartite negotiation rounds with government. The system of economic macro-tripartism is believed to achieve a high level of social consensus, political stability and international competitiveness and has proven a success story particularly in times of economic turbulence (Czada, 2004).

In recent years, the German corporatist system has been under steady attack. While it is true that, once instituted, principles of corporatist organization are remarkably resistant to any form of transformation pressure – be it internal or external –, some degree of reshaping can hardly be denied. At the macro level, labor unions face significant loss of membership while business associations find themselves being confronted by the emancipation of their single most crucial constituency. Large firms have begun lobbying the government outside the association channel and thus further propelled the downswing of associations in general. Drawing on recent research, scholars have denoted the ongoing erosion of macro-corporatism as a shift “from corporatism to lobbyism”14 (von Winter, 2004; von Alemann, 2000). This erosion also accounts for the growing variety of lobbying actors, including law firms, consultancies, and grassroots movements. Reasons for this development are manifold and include, but are not limited to, globalization, Europeanization (see footnote), social modernization, and pluralization. Changes in meso-corporatist arrangements, however, seem to be more strongly correlated to one single factor, corporate organization.

Industrial relations at the sector level, once again, reinforce institutional complementarities in coordinated market economies. A dense inter-firm corporate network has the capability to set wages across an industry and will thus reduce any incentive for a company to poach employees at a similar skill level from competitors. If wages vary across one sector, em-

---

14 One factor underpinning this development is Europeanization – here of a different kind. Since political decision-making has partly shifted away from the nation state to the EU, the institutional target structure of interest groups has changed and domestic authorities, while still important, have increasingly lost their attraction to interest groups (Lehmkuhl, 2006). Given the fact, though, that European institutions, primarily in the Commission, are accessible to all interest groups and not restricted to major federations only – as is the case in Germany – the fundamental openness allows member firms to bypass the ‘association channel’ and lobby the EU on their own. This ‘logic of access’ has been thoroughly studied by Bouwen (2002) who provides evidence for the ‘rise’ of large firms as important lobbying actors, which has significant implications for both the functioning and organization of associations at the domestic level (see also Steeck et al., 2006).
ployees with access to sensitive information such as production strategies will be willing to exploit the company’s vulnerability and ‘sell’ the information to a competitor. Hence companies want to cooperate and agree on sector-wide wages, working conditions and vocational training (Hall & Soskice, 2001). Now, the creation of a market for corporate control would “cut” this tie between companies. A market for corporate control, as present in LMEs, encourages firms to focus primarily on profit maximization and individual rationales. Wages are set according to market price mechanisms and employees might be subject to dismissal at any time (‘hire and fire’-principle). There is no need for intra-sectoral cooperation as it is fostered in CMEs. Furthermore, a market for corporate control implies an increase in hostile takeovers which would endanger the principle of mutual trust, a key condition for the stability of industrial relations. And finally, what would be the prospect of corporatist codetermination in a firm in which the shareholder has the final say?

Recent studies provide evidence for the notion that wage organization – confirming earlier expectations – has been decentralized and particularly shifted from multi-employer-bargaining to single-employer-bargaining (Traxler, 2004). This finding suggests a trend towards disorganization, which came up “when wage regulation came under neo-liberal pressure” (Traxler, 2004, p. 580). As Figure 2 shows, collective bargaining coverage has dramatically decreased over the past two decades and this trend is likely to continue. A comprehensive study undertaken by the WSI-Institute (2010) further suggests that firms have more and more tried to opt out of existing agreements, or when this was not possible have decided not to extend them.

Figure 2: Collective Bargaining Coverage in Germany 1998 – 2009, in % of all employees covered by an agreement

While Traxler (2004) urges us not to overemphasize these observations, as he believes path dependency will shield (macro-) corporatist arrangements from adjustment pressure, they still have significant implications for the system of industrial relations as a whole. For

http://scholarship.claremont.edu/urceu/vol2012/iss1/8
example, if wages are increasingly set at the firm- or plant-level rather than the industry- or sector level, one must assume that differences in salaries across a sector will sharply increase. In fact, studies have shown that the degree of wage centralization is a statistically relevant determinant of pay inequality (Wallerstein, 1999) and that sectoral wage differentials have gone an upward trend (Bellmann & Gartner, 2003).

Second, co-determination in privately owned companies both in West and East Germany has dropped from 41% in 1996 to 29% in 2011, according to recent data from the Hans Boeckler Foundation (2012). Finally, all that suggests that corporatism is eroding slowly not only at the macro- but also at the meso- and micro-levels of society.

5. Conclusion

Over the last several decades, the German state has undergone major changes. Basic aspects of the capitalist system have been affected by these changes and do not appear to shift back towards their past equilibrium. It comes somewhat as a surprise that the ‘German model’ has so profoundly eroded, given that scholars most commonly referred to Germany as a paradigm case for institutional stability and economic prosperity. The most striking evidence can be found for the decentralization of the financial system and the system of industrial relations, each connoting key features of Germany’s coordinated market economy. While these observations should not be overgeneralized, they clearly mark a trend towards convergence to the US model of capitalism.

What has this change caused and why are the various change processes obviously correlated? These were the two questions that served as a guideline through my paper, and I addressed them in the following way. First, the basic assumption underlying this paper was that not (only) internationalization has put adjustment pressure on Germany’s market economy, but Europeanization. I contended in favor of an analysis that aims at bringing the EU “back to the table” when searching for causes of domestic change. Unlike internationalization, I argued, Europeanization denotes a whole set of mechanisms that are at work to reshape the nation state. Europeanization is binding, has a larger magnitude and is politically intended, hence self-induced by the member states. Second, if one core element of a coordinated market economy is under attack, say by EU legislation, so are the others. Institutional complementarities as defined by the “Varieties of Capitalism” approach account for the high degree of mutual dependency between single elements of an economy and thus needs to be considered in such an analysis.

The present study contributes to the Europeanization debate in a way that links the debate to recent research in the field of capitalist diversity. Such an approach may not only help to broaden our understanding of the effects of EU integration; it also stresses the political dimension of the ‘clash of capitalisms’. Furthermore, the study advocates an alternative perspective to the debate on the erosion of corporatism in Germany. While it is widely believed that ‘societal modernization’ accounts for the slow yet steady decentralization of corporatist arrangements, this paper has traced change back to the micro-level of society. Because the EU has been extensively involved in creating a Europe wide market for corporate control, these developments have caused the German system of industrial relations (along with the financial system) to slowly fall apart. In fact, the ‘German Model’ as a whole is being faced with substantial adjustment pressure, and there is no reason to believe that this process will

15 In combination with a collective agreement
not forge ahead. If Europeanization continues the former German model is doomed to fade away in favor for a less just but more competitive system.

**AUTHOR’S NOTES**

This study was part of my senior thesis paper, which will be submitted to the University of Potsdam in July 2012. I would like to thank Professor Ron Rogowski (UCLA) for hosting this research and Cora Zeugmann for valuable comments.

**REFERENCES**


http://scholarship.claremont.edu/urceu/vol2012/iss1/8


Moravcsik, A. (1991). Negotiating the single European act: National interests and conven-
tional statecraft in the European community. *International Organization, 45*(1), 19-56.